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ORIGINAL

MEMORANDUM

TO: Docket Control

FROM: Ernest G. Johnson  
*for* Director  
Utilities Division

DATE: August 08, 2008

RE: RESPONSIVE STAFF REPORT FOR PICACHO PEAK WATER CO., INC. FOR A  
PERMANENT RATE INCREASE AND FOR AUTHORITY TO INCUR DEBT  
(DOCKET NO. W-02351A-07-0319 and W-02351A-07-0686)

Attached is the Responsive Staff Report for Picacho Peak Water Co., Inc.'s. Staff is filing this report to respond to the Company's Comments on Staff Report filed on June 9, 2008.

Any party who wishes may file comments to the Responsive Staff Report with the Commission's Docket Control by 4:00 p.m. on or before August 18, 2008.

EGJ:GWB:kdh

Originator: Gerald W. Becker

Arizona Corporation Commission

DOCKETED

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Service List for: Picacho Peak Water Company, Inc.  
Docket No. W-02351A-07-0319 & W-02351A-07-0686

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**RESPONSIVE STAFF REPORT  
UTILITIES DIVISION  
ARIZONA CORPORATION COMMISSION**

**PICACHO PEAK WATER CO., INC.**

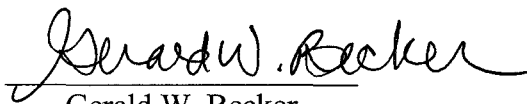
**DOCKET NO. W-02351A-07-0319 and W-02351A-07-0686**

**APPLICATION FOR A  
PERMANENT RATE INCREASE AND  
AUTHORITY TO INCUR DEBT**

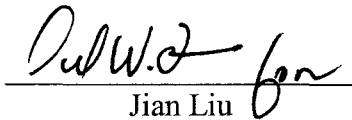
**AUGUST 8, 2008**

## STAFF ACKNOWLEDGMENT

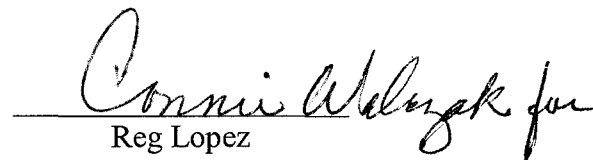
The Responsive Staff Report for Picacho Peak Water Co., Inc., Docket Nos. W-02351A-07-0319 and W-02351A-07-0686, is the responsibility of the Staff members listed below. Gerald W. Becker is responsible for the review and analysis of the Company's application, recommended revenue requirement, rate base, and rate design. Jian Liu is responsible for the engineering and technical analysis. Reg Lopez is responsible for analysis of complaints, inquires, opinions, and any other consumer data relative to this case.



Gerald W. Becker  
Public Utility Analyst V



Jian Liu  
Utilities Engineer



Reg Lopez  
Public Utilities Consumer Analyst II

**EXECUTIVE SUMMARY  
RESPONSIVE STAFF REPORT  
PICACHO PEAK WATER CO., INC.  
W-02351A-07-0319 & W-02351A-07-0686**

Picacho Peak Water Co., Inc. ("Company") is located near Picacho Peak. The Company is engaged in the business of providing utility water service to 5 residential and 9 commercial customers.

On December 13, 2007, the Company filed an application for a permanent rate increase. Staff sent a Deficiency Notice on January 14, 2008 and a Letter of Sufficiency on March 20, 2008. Picacho also filed a Finance Application on May 22, 2007, and an Amended Finance Application on December 13, 2007. A Procedural Order, dated February 14, 2008, granted Picacho's January 29, 2008 request to consolidate the rate and financing applications. Staff filed its Staff Report on May 21, 2008, and the Company filed its comments on Staff Report on June 9, 2008. On July 11, 2008, the Hearing Division issued a Procedural Order which ordered Staff to file its response to the Company's comments by August 8, 2008. This Responsive Staff Report reflects Staff's updated position after reviewing and considering the Company's comments.

The Company's rate application, as amended by its comments of June 9, 2008, requested a revenue increase of \$34,296, a 107.75 percent over test year revenue of \$31,828. The Company's proposed rates, as filed, produce operating revenues of \$66,124 and result in an operating income of \$31,029 for a rate of return of 900.44 percent and an operating margin of 46.93 percent. The Company's requested rates would increase the typical 3/4-inch meter residential bill with a median usage of 7,750 gallons from \$31.15 to \$42.12, an increase of \$10.97 or 35.2 percent. The Company also requested authorization to obtain a \$150,000 20-year amortizing loan from the Water Infrastructure Finance Authority of Arizona ("WIFA") for remediation of excess levels of nitrates and coliform.

Staff recommends a \$34,572 or 108.6 percent increase over test year revenue of \$31,828. Staff's recommended revenues of \$66,400 would result in an operating income of \$30,878, a rate of return of 58.52, percent and an operating margin of 46.50 percent. Staff's recommended revenues and income are necessary to satisfy the covenants of the Company's proposed \$150,000 WIFA loan. Staff's recommended rates would increase the typical 3/4-inch meter residential bill with a median usage of 7,750 gallons from \$31.15 to \$45.91 for an increase of \$14.76, or 47.4 percent.

Staff recommends:

- Approval of Staff's rates and charges as shown in Schedule GWB-4. In addition to collection of its regular rates and charges, the Company may collect from its customers a proportionate share of any privilege, sales, or use tax per Commission Rule (14-2-409D.5).

- That rates not become effective until the Company has either become current on its property tax obligations or has a final payment plan negotiated with Pinal County and has filed verification with Docket Control.
- That the Commission order the Company to maintain its records in accordance with the National Association of Regulatory Utility Commissioners ("NARUC") Uniform System of Accounts ("USOA").
- That the Company be ordered to install and maintain operable metering devices for its well and for all customers and file with Docket Control, as a compliance item in this docket, within 90 days after the Decision in this matter is issued, an affidavit stating that the required operable metering devices have been installed.
- Authorization of the depreciation rates shown in Table B of the Engineering Report.
- That Picacho Peak file each January and July a report covering the previous six months that contains all activities regarding the ADEQ's Consent Order. The written report should continue until Staff receives notice that the Picacho Peak water system is in total compliance with ADEQ regulations.
- That the Company file with Docket Control, as a compliance item in this docket, a schedule of its approved rates and charges within 30 days after the Decision in this matter is issued.
- That the Company file a subsequent rate case using a test year ending December 31, 2010, no later than June 01, 2011. If the Company finds it necessary, it may file a rate case sooner with an earlier test year.
- That the Company file a curtailment tariff in the form found on the Commission's website at [www.azcc.gov/divisions/utilities/forms/cross\\_c.pdf](http://www.azcc.gov/divisions/utilities/forms/cross_c.pdf). The tariff shall be docketed as a compliance item in this docket within 45 days of the effective date of the order in this proceeding for review and certification by Staff.
- That the Company obtain information for its Distribution Mains and report it in its next Annual Report (due April 2009).
- That the Company must be in full compliance with ADEQ by December 31, 2009. If not, Staff should be required to file an Order to Show Cause against the Company.
- That the Commission authorize the Company to obtain an 18-to-22-year amortizing loan at a rate not to exceed the prime rate plus 2 percent (currently 7.00 percent) for an amount not to exceed \$150,000 to finance remediation improvements subject to the condition that the Company files with Docket Control an affidavit verifying customer notice.
- Authorizing the Company to engage in any transactions and to execute any documents necessary to effectuate the authorizations granted.

- That a copy of the executed loan documents be filed with Docket Control, as a Compliance item in this docket, within 60 days of the execution of any transactions.

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## **Attachment**

Engineering Report-Rate Case.....	Attachment A
Engineering Report-Financing.....	Attachment B

## **RATE CASE**

### **Fact sheet**

**Current Rates:** Decision No. 53169, dated August 11, 1982.

**Type of Ownership:** Arizona "C" Corporation, Nonprofit.

**Location:** The Company serves 5 residential, 9 commercial (1 RV park with over 200 spaces) near Picacho Peak, AZ.

### **Rates:**

Permanent rate increase application filed: December 13, 2007; Deficiency Notice sent January 14, 2008; and Letter of Sufficiency sent March 20, 2008. Picacho also filed a Finance Application on May 22, 2007 and an Amended Finance Application on December 13, 2007. A Procedural Order, dated February 14, 2008, granted Picacho's January 29, 2008, request to consolidate the rate and financing applications. Picacho filed comments amending its rate request on June 9, 2008.

Current Test Year Ended: December 31, 2006.

	<u>Company Current Rates</u>	<u>Company Proposed Rates</u>	<u>Staff Recommended Rates</u>
Monthly Minimum Charge:			
Residential			
5/8 x 3/4-inch meter	\$15.00	N/A	\$15.00
3/4 inch meter	N/A	\$20.00	\$15.00
Gallons in Minimum	3,000	0	0
Commercial			
5/8 x 3/4-inch meter	\$15.00	N/A	\$138.00
3/4-inch meter	\$85.00	\$80.00	\$138.00
Gallons in Minimum	3,000	0	0
2-inch meter	\$85.00	\$500.00	\$1425.00
Gallons in Minimum	3,000	0	0
Commodity Charge:			
All Customers			
Excess of minimum, per 1,000 gallons	\$3.40		

	<u>Company Current Rates</u>	<u>Company Proposed Rates</u>	<u>Staff Recommended Rates</u>
Residential Customers:			
All 3/4-inch and 5/8 x 3/4-inch meters:			
Tier One 1 to 5,000 gallons		\$2.50	N/A
Tier Two 5,001 to 15,000 gallons		\$3.50	N/A
Tier Three 15,001 gallons to infinite		\$4.90	N/A
All 3/4-inch and 5/8 x 3/4-inch meters:			
Tier One 1 to 3,000 gallons		N/A	\$3.05
Tier Two 3,001 to 10,000 gallons		N/A	\$4.58
Tier Three 10,001 gallons to infinite		N/A	\$5.49
Commercial			
All 3/4-inch and 5/8 x 3/4-inch meters:			
Tier One 1 to 10,000 gallons		\$7.25	\$4.58
Tier Two 10,001 to infinite		\$8.69	\$5.49
Commercial 2 inch meter:			
Tier One 1 to 25,000 gallons		\$7.25	\$4.58
Tier Two 25,001 to infinite		\$8.69	\$5.49
Typical residential bill (Based on median usage of 7,750 gallons)	\$31.15	\$42.12	\$45.91

### **Customers:**

The number of customers is mostly static. During the test year there were 5 residential customers on 3/4-inch meters, and Company billed its customers at the 5/8 x 3/4-inch meter tariff rate during the test year. Also, there are 8 commercial customers on 3/4-inch meters and 1 commercial customer with a broken 2-inch meter supplying water to over 200 RV spaces.

### **Notification:**

Customer Notification was mailed December 13, 2007.

### **Complaints:**

There were no opinions filed regarding the rate increase.

### **Summary of Filing**

The test year results, as adjusted by Arizona Corporation Commission ("Commission") Utilities Division Staff ("Staff"), show that Picacho Peak Water Company, Inc ("Picacho" or "Company") realized total operating revenue of \$31,828 and an operating loss of \$3,694, for no operating margin as shown in Schedule GWB-1.

The Company's proposed rates, as amended by the June 9, 2008 comments, produce operating revenues of \$66,124, for a \$31,029 operating income, a 46.93 percent operating margin and a 900.44 percent rate of return on a \$3,446 rate base. The Company's requested rates would increase the typical 3/4-inch meter residential bill with a median usage of 7,750 gallons from \$31.15 to \$42.12 for an increase of \$10.97 or 35.2 percent as shown in Schedule GWB-5, page 1 of 3.

Staff recommends a \$34,572, or 108.6 percent increase over test year revenue of \$31,828. Staff's recommended revenues of \$66,400 would result in a \$30,878 operating income, a 46.50 percent operating margin, and a 58.52 percent rate of return on a \$52,768 rate base. Staff's recommended rates would increase the typical 3/4-inch meter residential bill with a median usage of 7,750 gallons from \$31.15 to \$45.91, an increase of \$14.76 or 47.4 percent. Staff's recommended revenues and income are necessary to satisfy the covenants of the Company's proposed \$150,000 Water Infrastructure Finance Authority of Arizona ("WIFA") loan.

### **Background**

On December 13, 2007, Picacho filed an application for a permanent rate increase. Staff sent a Deficiency Notice on January 14, 2008. In addition, Picacho had previously filed a Finance Application on May 22, 2007, and an Amended Finance Application on December 13, 2007. A Procedural Order, dated February 14, 2008, granted Picacho's January 29, 2008, request to consolidate the rate and financing applications. Staff issued a Letter of Sufficiency on March 20, 2008. Staff filed its Staff Report on May 21, 2008, and the Company filed its comments on the Staff Report on June 9, 2008. On July 11, 2008, the Hearing Division issued a Procedural Order which ordered Staff to file its response to the Company's comments by August 8, 2008. This Responsive Staff Report reflects Staff's updated position after reviewing and considering the Company's comments.

### **Consumer Services**

A review of the Commission's records revealed the following customer complaints and inquiries from Year 2005 – zero complaints, one inquiry; Year 2006 – zero complaints and zero inquiries; Year 2007 – zero complaints, two inquiries; Year 2008 - zero complaints and zero inquiries. All complaints and inquiries have been resolved and closed.

### **Compliance**

A check with the Utilities Division Compliance Section showed no outstanding compliance issues.

The Company is current on its sales tax payments, but not in its property taxes. The Company is negotiating a payment plan for its property taxes with Pinal County.

The Company is in good standing with the Corporations Division of the Commission.

The Arizona Department of Environmental Quality ("ADEQ") has determined that this system is currently not delivering water that meets water quality standards as required by the Arizona Administrative Code, Title 18, Chapter 4 due to the levels of nitrates and coliform. To remediate this, the Company has submitted an application seeking authority to incur \$150,000 of debt from WIFA. The quality issues are discussed further in the attached Engineering Report.

Staff's review of the Company's books and records revealed that they are not kept in accordance with the National Association of Regulatory Utility Commissioners ("NARUC") Uniform System of Accounts ("USOA").

### **Engineering Analysis**

Staff's Engineering Report is attached. There are six recommendations included in the Staff Recommendations section. The first and third recommendations relate to depreciation rates and service line and meter installation charges. The second recommendation relates to annual water testing expenses, the amount of which is reflected in the Staff's financial review of the application for the rate increase. The fourth recommendation relates to a broken well meter which precluded Staff from calculating system water losses. Staff also determined that the meter serving the one commercial customer with a 2-inch meter is also broken. The combination of unmetered water at both the source and at one customer's premises prevented Staff from confirming or reliably estimating the amount of water delivered to the customer with the 2-inch meter. The fifth recommendation relates to excessive levels of nitrates and coliform in the water. The sixth recommendation asks that Picacho file a curtailment tariff.

In response to the Company's June 9, 2008 comments, Staff agrees with the Company's request under section 3.1 Meter Installations to allow the Company 90 days to install appropriate metering devices. This is consistent with Engineering Memo dated May 12, 2008.

Also in response to the Company's comments regarding Section 3.2 Distribution System Data, Staff reaffirms that it is important to have documentation showing the Company's water distribution system. Staff would suggest that the Company perform a data search for the original distribution system as-built information by contacting its design engineers, contractors, and/or government agencies, such as ADEQ, before spending \$30k to \$60k to recreate the data.

### **Rate Base**

Staff recommends three adjustments that in aggregate increase the Company's proposed rate base by \$49,322, from \$3,446 to \$52,768 as shown in Schedule 2, page 1. Details of Staff's adjustments are presented below.

Accumulated Depreciation - Adjustment A decreases accumulated depreciation by \$34,944, from \$148,353 to \$113,409, as shown in Schedule 2, Page 1. Staff's adjustment reflects the application of correct depreciation as authorized in Decision No. 53169 for the intervening years.

Accumulated Amortization of CIAC - Adjustment B increases this account by \$10,946, from \$0 to \$10,946 as shown on Schedule 2, Page 1. Staff's adjustment reflects amortization of the Gross CIAC balance that should have been recorded for the years 1982 through 2006.

Working Capital - Adjustment C provides a cash working capital allowance of \$3,432, based on the formula method, as shown on Schedule 2, page 1. The formula method recognizes one-eighth of the operating expenses excluding depreciation, taxes, purchased power expenses plus one twenty-fourth of purchased power expenses. Picacho did not claim a cash working capital allowance.

### **Operating Income**

Staff recommends five adjustments that in aggregate decrease the test year operating result from the Company's proposed by \$427 from a \$3,267 loss to a \$3,694 loss as shown in Schedule 3, page 1. Details of Staff's adjustments are presented below.

### **Operating Expenses**

Outside Services - Adjustment A decreases this account by \$750 from \$17,722 to \$16,972 to remove expenses that are not supported by documentation, as shown on Schedule 3, page 1 and 2.

Water Testing - Adjustment B increases this account by \$721 from \$778 to \$1,499 to reflect Staff's determination of the Company's annual water testing cost, as shown in Schedule 3, page 1 and 2.

Miscellaneous Expense - Adjustment C decreases this account by \$145 to zero to remove expenses that are not supported by documentation, as shown in see Schedule 3, page 2.

Depreciation Expense - Adjustment D increases this account by a net of \$504 to reflect application of Staff's recommended depreciation rates to Staff's recommended plant balances less any fully depreciated or non-depreciable plant and offset by CIAC amortization. The

calculation of Staff's recommended depreciation expense and adjustment is shown in Schedule 3, page 2.

Property Taxes – Adjustment E increases this amount by \$97 from \$2,922 to \$3,019, to equal the amounts indicated in the supporting documentation. See Schedule 3, pages 1 and 2.

### **Revenue Requirement**

Staff recommends a \$34,572 or 108.6 percent increase over test year revenue of \$31,828. Staff's recommended revenues of \$66,400 would result in a \$30,878 operating income, a 46.50 percent operating margin, and a 58.52 percent rate of return on a \$52,768 rate base. Staff's recommended revenues and income are necessary to satisfy the covenants of the Company's proposed \$150,000 WIFA loan.

### **Rate Design**

Schedule GWB-4 presents a complete list of the Company's present, proposed, and Staff's recommended rates and charges.

The present rate design has a single tier structure, i.e., uniform commodity rate, with 3,000 gallons included in the minimum monthly charge for all meter sizes. The minimum monthly charges are as follows: residential 5/8 x 3/4-inch meter, \$15.00; and commercial – all meter sizes \$85.00.

The Company proposes an inverted three-tier rate design with a discounted commodity rate for its 5 residential customers on 3/4-inch meters, zero gallons included in the minimum monthly charge and break-over points at 5,000 and 15,000 gallons for its residential customers. For its 8 commercial customers on 3/4-inch meters, the Company proposes an inverted two-tier rate design, zero gallons included in the minimum monthly charge, and a break-over point at 25,000 gallons. For its sole commercial customer on a 2-inch meters, the Company proposes an inverted two-tier rate design, zero gallons included in the minimum monthly charge and a break-over point at 25,000 gallons. The Company proposes the following minimum monthly charges: residential 3/4-inch meter, \$20.00; commercial 3/4-inch meter, \$80.00; and commercial 2-inch meter, \$500.00. The Company's proposed rates would increase the typical 3/4-inch meter residential bill with a median usage of 7,750 gallons from \$31.15 to \$42.12 for an increase of \$10.97 or 35.2 percent.

Staff recommends a three-tier inverted rate structure for 5/8 x 3/4-inch and 3/4-inch meters and a two-tier inverted rate structure for larger meters. The breakover points for 5/8 x 3/4-inch and 3/4-inch meters are at 3,000 and 10,000 gallons. The breakover points for the larger meters graduate with size. Staff's recommended minimum monthly charges for 5/8 x 3/4-inch and 3/4-inch meters are as follows: residential 5/8 x 3/4-inch meter, \$15.00; residential 3/4-inch meter, \$15.00; commercial 5/8 x 3/4-inch meter, \$138.00; commercial 3/4-inch meter, \$138.00 and \$1,425.00 for the commercial 2-inch customers. The difference between the

minimum charges for the commercial versus residential customers is based on the Company's representation of the disproportionate cost of improving the water quality for respective customer classes. The residential customers will be provided with point of use reverse osmosis systems, while the commercial customers will require large, on site reverse osmosis plants. Staff determined that its recommended \$34,572 increase should be allocated in the amounts of \$2,544, \$11,941 and \$20,087 to the residential, ¾-inch commercial and 2-inch commercial classes, respectively. For this reason, Staff is recommending significantly different percentage increases for each class of customer. Staff further recommends minimum monthly rates for larger meters that graduate with size.

Staff's recommended rates would increase the typical ¾-inch meter residential bill with a median usage of 7,750 gallons from \$31.15 to \$45.91 for an increase of \$14.76 or 47.4 percent.

Presently, the Company does not have any Service Line, Meter Installation, or other fees such as Establishment fees on record. The Company is proposing combined Service Line and Meter Installation Charges. The proposed charges are less than the typical range recommended by Staff. Staff recommends adoption of the Company's total proposed charges but recommends rates that segregate the total by each component, i.e., Service Line and Meter Installation Charges as shown in Schedule GWB-4.

The Company proposes to increase Establishment Service Charge from \$0.00 to \$25.00. Staff finds \$25.00 as a reasonable and normal charge.

The Company proposes to increase Establishment Service Charge (After Hours) from \$0.00 to \$35.00. Staff recommends \$35.00 as being reasonable and normal.

The Company proposes to increase Reconnection of delinquent account from \$0.00 to \$25.00. Staff recommends \$25.00 as being reasonable and normal.

The Company proposes to increase Reconnection of delinquent account (After Hours) from \$0.00 to \$35.00. Staff recommends \$35.00 as being reasonable and normal.

The Company proposed to increase Meter Re-read (if correct) from \$0.00 to \$10.00. Staff finds \$10.00 as a reasonable and normal charge.

The Company proposed to increase Meter Test (if correct) from \$0.00 to \$25.00. Staff finds \$25.00 as a reasonable and normal charge.

The Company proposes to increase service charges for Reconnection (delinquent) from \$0.00 to \$25.00. Staff finds \$25.00 as a reasonable and normal.

The Company proposed to establish a Late Fee at 1.00 percent. Staff recommends a charge of 1.0% per month on delinquent bills.



The Company proposed to establish a Deferred Payment Fee of 1.50 percent. Staff recommends a fee of 1.50% per month and that the Company follow Commission Rules regarding Deferred Payments (AAC R-14-2-409.G).

The Company proposes to increase its Non Sufficient Fund charges from \$0.00 to \$25.00. Staff finds \$25.00 as a reasonable and normal charge.

The Company proposes and Staff recommends that deposits and deposit interest be set according to AAC R-14-2-403(B).

The Company proposes and Staff recommends that charges for re-establishment within 12 months be determined by the number of months off system times the monthly minimum per commission Rule AAC R-14-2-403(D).

### **Staff Recommendations - Rates**

Staff recommends:

- Approval of Staff's rates and charges as shown in Schedule GWB-4. In addition to collection of its regular rates and charges, the Company may collect from its customers a proportionate share of any privilege, sales, or use tax per Commission Rule (14-2-409D.5).
- That rates not become effective until the Company has either become current on its property tax obligations or has a final payment plan negotiated with Pinal County and has filed verification with Docket Control.
- That the Commission order the Company to maintain its records in accordance with the National Association of Regulatory Utility Commissioners ("NARUC") Uniform System of Accounts ("USOA").
- That the Company be ordered to install and maintain operable metering devices for its well and for all customers and file with Docket Control, as a compliance item in this docket, within 90 days after the Decision in this matter is issued, an affidavit stating that the required operable metering devices have been installed.
- Authorization of the depreciation rates shown in Table B of the Engineering Report.
- That Picacho Peak file each January and July a report covering the previous six months that contains all activities regarding the ADEQ's Consent Order. The written report should continue until Staff receives notice that the Picacho Peak water system is in total compliance with ADEQ regulations.

- That the Company file with Docket Control, as a compliance item in this docket, a schedule of its approved rates and charges within 30 days after the Decision in this matter is issued.
- That the Company file a subsequent rate case using a test year ending December 31, 2010, no later than June 01, 2011. If the Company finds it necessary, it may file a rate case sooner with an earlier test year.
- That the Company file a curtailment tariff in the form found on the Commission's website at [www.azcc.gov/divisions/utilities/forms/cross\\_c.pdf](http://www.azcc.gov/divisions/utilities/forms/cross_c.pdf). The tariff shall be docketed as a compliance item in this docket within 45 days of the effective date of the order in this proceeding for review and certification by Staff.
- That the Company obtain information for its Distribution Mains and report it in its next Annual Report (due April 2009).
- That the Company must be in full compliance with ADEQ by December 31, 2009. If not, Staff should be required to file an Order to Show Cause against the Company.

## **FINANCING**

### **Introduction**

On May 22 2007, Picacho filed a financing application with the Commission requesting authorization to obtain a \$150,000 20-year amortizing loan from WIFA.

Picacho's engineering cost estimate for all of the proposed capital improvements is \$150,000 which will ultimately be used to install reverse osmosis systems at specific points where drinking water is most likely to be dispensed. Residential customers will be provided with point of use reverse osmosis systems, while the commercial customers will require large, on site reverse osmosis plants.

### **Public Notice**

Picacho included a proposed notice in its application but has not provided a proof of notice to Staff.

### **Purpose and Terms of the Proposed Financing**

The Company is requesting authority to borrow \$150,000 from WIFA at 5 percent for 20 years. The amount is estimated based on general discussions that the Company had with ADEQ, consulting engineers and vendors of the treatment equipment. The Company plans to use the funds to:

- Retain an engineer to develop a more specific work plan to determine the exact treatment plant size, location, and capacity for each customer.
- Install the recommended reverse osmosis systems at specific points where drinking water is most likely to be dispensed.

### **Engineering Analysis**

Staff examined the application and determined that that estimate is a good starting point but notes that the Company does not have a detailed work plan. Staff makes no "used and useful" determination of the proposed plant and no particular future treatment should be inferred for rate-making or rate base purposes.

### **Financial Analysis**

Staff's analysis is based on Picacho's financial statements dated December 31, 2006. The financial analysis shown in Schedule GWB-6 presents selected financial information from the financial statements and the pro forma effect of a \$150,000 loan with Staff's recommended revenues and expenses from the rate case. Schedule GWB-6 also shows the capital structure and debt service coverage ("DSC") and times interest earned ("TIER") ratios.

### **Capital Structure**

At December 31, 2006, Picacho's capital structure consisted of 2.3 percent short-term debt, 56.9 percent long-term debt, and 40.7 percent equity. A pro forma capital structure recognizing issuance of a \$150,000 20-year amortizing loan is composed of 2.7 percent short-term debt, 82.8 percent long-term debt and 14.6 percent equity as shown in Schedule GWB-6.

### **Interest and Debt Service Coverage**

Staff also examined the effects of the proposed financing on the Company's TIER and DSC.

DSC represents the number of times internally generated cash (i.e., earnings before interest, income tax, depreciation and amortization expenses) covers required principle and interest payments on debt. A DSC greater than 1.0 means operating cash flow is sufficient to cover debt obligations.

TIER represents the number of times earnings before income tax expense covers interest expense on debt. A TIER greater than 1.0 means that operating income is greater than interest expense. A TIER less than 1.0 is not sustainable in the long term but does not necessarily mean that debt obligations cannot be met in the short term.

Schedule GWB-6 shows that for the year ending December 31, 2006, Picacho had immeasurable TIER and DSC amounts due to the Company's negative earnings. Staff's pro forma analysis shows that Staff's recommended revenue and issuance of a \$150,000, 20-year, 5.44 percent amortizing loan results in a 1.76 TIER and 1.25 DSC. The pro forma DSC shows that Picacho would have adequate cash flow to meet all obligations.

### **Conclusions and Recommendations - Financing**

Staff concludes that the proposed WIFA loan is an appropriate financial instrument to finance the proposed remediation plant. Staff further concludes that issuance of a long-term amortizing loan of approximately 20-years for the \$150,000 estimated cost of the capital improvements is appropriate, is within its corporate powers, is compatible with the public interest, would not impair its ability to provide services and would be consistent with sound financial practices.

Staff recommends that the Commission authorize Picacho to obtain an 18-to-22-year amortizing loan at a rate not to exceed the prime rate plus 2 percent (currently 7.00 percent) for an amount not to exceed \$150,000 to finance remediation improvements subject to the condition that the Company files with Docket Control an affidavit verifying customer notice.

Staff further recommends authorizing Picacho to engage in any transactions and to execute any documents necessary to effectuate the authorizations granted.

Staff further recommends that a copy of the executed loan documents be filed with Docket Control, as a Compliance item in this docket, within 60 days of the execution of any transactions.

## RATE BASE

	----- Original Cost -----		
	Company	Adjustment	Staff
Plant in Service	\$169,204	\$0	\$169,204
Less:			
Accum. Depreciation	148,353	(34,944) A	113,409
<b>Net Plant</b>	<b>\$20,851</b>	<b>\$34,944</b>	<b>\$55,795</b>
Less:			
Plant Advances	\$0	\$0	\$0
Accumulated Deferred Income Taxes	0	0	0
<b>Total Advances</b>	<b>\$0</b>	<b>\$0</b>	<b>\$0</b>
Contributions Gross	\$17,405	\$0	\$17,405
Less:			
Amortization of CIAC	0	10,946 B	10,946
<b>Net CIAC</b>	<b>\$17,405</b>	<b>(\$10,946)</b>	<b>\$6,459</b>
<b>Total Deductions</b>	<b>\$17,405</b>	<b>(\$10,946)</b>	<b>\$6,459</b>
Plus:			
1/24 Power	\$0	\$181 C	\$181
1/8 Operation & Maint.	0	3,252 C	3,252
Inventory	0	0	0
Prepayments	0	0	0
<b>Total Additions</b>	<b>\$0</b>	<b>\$3,432</b>	<b>\$3,432</b>
<b>Rate Base</b>	<b>\$3,446</b>	<b>\$49,322</b>	<b>\$52,768</b>

*Explanation of Adjustment:*

- A Schedule GWB-2 Page 2
- B Schedule GWB-2 Page 3
- C Formula Method to Calculate Working Capital

<b>ACCUMULATED DEPRECIATION ADJUSTMENT</b>
--

		<u>Amount</u>	
Accumulated Depreciation - Per Company		\$ 148,353	
Accumulated Depreciation - Per Staff		<u>113,409</u>	A
<b>Total Adjustment</b>		<u><b>(\$34,944)</b></u>	
<u>Explanation of Adjustment:</u>			
<u>Acct. No.</u>	<u>Description</u>		
304	Structures & Improvements	\$ 2,544	
	Per Staff	<u>1,364</u>	<u>\$ (1,180)</u>
	To recognize depreciation rates authorized in Decision No. 53169, August 11, 1982.		
330.1	Storage Tanks	\$ 42,311	
	Per Staff	<u>22,266</u>	<u>\$ (20,045)</u>
	To recognize depreciation rates authorized in Decision No. 53169, August 11, 1982.		
331	Transmission and Distribution Mains	\$ 45,253	
	Per Staff	<u>31,943</u>	<u>\$ (13,310)</u>
	To recognize depreciation rates authorized in Decision No. 53169, August 11, 1982.		
334	Meters and Meter Installations	1997	
	Per Staff	<u>1588</u>	<u>\$ (409)</u>
	To recognize depreciation rates authorized in Decision No. 53169, August 11, 1982.		

<b>CIAC AND WORKING CAPITAL ADJUSTMENTS</b>
---

	<u>Amount</u>
Accumulated Amortization - Per Company	\$ -
Accumulated Amortization - Per Staff	<u>10,946 B</u>
<b>Total Adjustment</b>	<b><u>\$10,946</u></b>
<u>Explanation of Adjustment:</u>	

Ref B	Amortization of CIAC using yearly composite depreciation expense rates.		
	<u>Amount</u>	<u>Cumulative</u>	<u>Remaining</u>
Beginning Balance - 1981			\$ 17,405
1982	\$ 429	\$ 429	16,976
1983	\$ 429	858	16,547
1984	\$ 429	1,287	16,118
1985	\$ 429	1,716	15,689
1986	\$ 402	2,118	15,287
1987	\$ 420	2,538	14,867
1988	\$ 420	2,959	14,446
1989	\$ 420	3,379	14,026
1990	\$ 422	3,801	13,604
1991	\$ 483	4,284	13,121
1992	\$ 470	4,754	12,651
1993	\$ 460	5,214	12,191
1994	\$ 520	5,734	11,671
1995	\$ 484	6,218	11,187
1996	\$ 559	6,777	10,628
1997	\$ 557	7,335	10,070
1998	\$ 557	7,892	9,513
1999	\$ 504	8,396	9,009
2000	\$ 505	8,901	8,504
2001	\$ 505	9,406	7,999
2002	\$ 400	9,806	7,599
2003	\$ 285	10,091	7,314
2004	\$ 285	10,376	7,029
2005	\$ 285	10,661	6,744
2006	\$ 285	<u>\$ 10,946</u>	<u>\$ 6,459</u>

**Pichaco Peak Water Company**

Docket Nos. W-01877A-07-0686 &amp; 07-0319

Test Year Ended December 31, 2006

Schedule GWB-3

Page 1 of 2

**STATEMENT OF OPERATING INCOME**

	Company Exhibit	Staff Adjustments	Staff Adjusted
<u>Revenues:</u>			
461 Metered Water Revenue	\$31,828	\$0	\$31,828
460 Unmetered Water Revenue	0	0	0
474 Other Water Revenues	0	0	0
<b>Total Operating Revenue</b>	<b>\$31,828</b>	<b>\$0</b>	<b>\$31,828</b>
<u>Operating Expenses:</u>			
601 Salaries and Wages	\$0	\$0	\$0
610 Purchased Water	0	0	0
615 Purchased Power	4,333	0	4,333
618 Chemicals	0	0	0
620 Repairs and Maintenance	0	0	0
621 Office Supplies & Expense	0	0	0
630 Outside Services	17,722	(750) A	16,972
635 Water Testing	778	721 B	1,499
641 Rents	0	0	0
650 Transportation Expenses	0	0	0
657 Insurance - General Liability	1,620	0	1,620
659 Insurance - Health and Life	0	0	0
666 Regulatory Commission Expense - Rate Case	5,921	0	5,921
675 Miscellaneous Expense	145	(145) C	0
403 Depreciation Expense	1,609	504 D	2,113
408 Taxes Other Than Income	0	0	0
408.11 Property Taxes	2,922	97 E	3,019
409 Income Tax	45	0	45
<b>Total Operating Expenses</b>	<b>\$35,095</b>	<b>\$427</b>	<b>\$35,522</b>
<b>OPERATING INCOME/(LOSS)</b>	<b>(\$3,267)</b>	<b>(\$427)</b>	<b>(\$3,694)</b>
<u>Other Income/(Expense):</u>			
419 Interest and Dividend Income	\$0	\$0	\$0
421 Non-Utility Income	0	0	0
427 Interest Expense	3,078	0	3,078
4XX Reserve/Replacement Fund Deposit	0	0	0
426 Miscellaneous Non-Utility Expense	0	0	0
<b>Total Other Income/(Expense)</b>	<b>(\$3,078)</b>	<b>\$0</b>	<b>(\$3,078)</b>
<b>NET INCOME/(LOSS)</b>	<b>(\$6,345)</b>	<b>\$ (427)</b>	<b>(\$6,772)</b>



<b>STAFF ADJUSTMENTS</b>
--------------------------

A	OUTSIDE SERVICES - Per Company	\$17,722	
	Per Staff	16,972	(\$750)
	To remove undocumented expenses.		
B	WATER TESTING - Per Company	\$778	
	Per Staff	1,499	\$721
	To reflect normalized ongoing water testing expenses.		
C	MISCELLANEOUS EXPENSE - Per Company	\$145	
	Per Staff	0	(\$145)
	To remove undocumented expenses.		
D	DEPRECIATION - Per Company	\$1,609	
	Per Staff	2,113	\$504

*Explanation of Adjustment:*

**Pro Forma Annual Depreciation Expense:**

Plant in Service	\$169,204
Less: Non Depreciable Plant	500
Fully Depreciated Plant	65,867
Depreciable Plant	\$102,837
Times: Staff Proposed Depreciation Rate	varies
Credit to Accumulated Depreciation	\$2,548 *
Less: Amort. of CIAC* @ 2.50%	435
<b>Pro Forma Annual Depreciation Expense</b>	<b>\$2,113</b>

**\* Amortization of CIAC:**

Contribution(s) in Aid of Construction (Gross)	\$17,405
Less: Non Amortizable Contribution(s)	0
Fully Amortized Contribution(s)	0
Amortizable Contribution(s)	\$17,405
Times: Staff Proposed Amortization Rate	2.50%
<b>Amortization of CIAC</b>	<b>\$435</b>

E	PROPERTY TAXES - Per Company	\$2,922	
	Per Staff	3,019	\$97
	To record 2006 property documentation.		

Monthly Usage Charge	RATE DESIGN		
	Present Rates	-Proposed Rates-	
		Company	Staff
Residential:			
5/8" x 3/4" Meter - Residential	\$ 15.00	\$ -	\$ 15.00
3/4" Meter - Residential	\$ -	\$ 20.00	\$ 15.00
1" Meter	\$ -	\$ -	\$ 37.50
1½" Meter	\$ -	\$ -	\$ 75.00
2" Meter	\$ -	\$ -	\$ 120.00
3" Meter	\$ -	\$ -	\$ 240.00
4" Meter	\$ -	\$ -	\$ 375.00
6" Meter	\$ -	\$ -	\$ 750.00
Commercial			
5/8" x 3/4" Meter - Commercial	\$ 85.00	\$ -	\$ 138.00
3/4" Meter - Commercial	\$ -	\$ 80.00	\$ 138.00
1" Meter	\$ -	\$ -	\$ 345.00
1½" Meter	\$ -	\$ -	\$ 690.00
2" Meter - Commercial	\$ 85.00	\$ 500.00	\$ 1,425.00
3" Meter	\$ -	\$ -	\$ 2,208.00
4" Meter	\$ -	\$ -	\$ 3,450.00
6" Meter	\$ -	\$ -	\$ 6,900.00
Commodity Rates			
Gallons Included in Minimum (000's)	3	0	0
Excess of Minimum - per 1,000 Gallons	\$3.40	\$0.00	\$0.00
Company -			
3/4 - inch meter - Residential			
Tier One up to 5,000 Gallons		\$ 2.50	
Tier Two from 5,001 to 15,000 Gallons		\$ 3.50	
Tier Three - over 15,000 Gallons		\$ 4.90	
Staff 3/4 - inch meter - Residential			
Tier One up to 3,000 Gallons	N/A		\$ 3.05
Tier Two from 3,001 to 10,000 Gallons	N/A		\$ 4.58
Tier Three - over 10,000 Gallons	N/A		\$ 5.49
Staff			
5/8 x 3/4 - inch meter - Residential			
Tier One up to 3,000 Gallons	N/A	N/A	\$ 3.05
Tier Two from 3,001 to 10,000 Gallons	N/A	N/A	\$ 4.58
Tier Three - over 10,000 Gallons	N/A	N/A	\$ 5.49
5/8 x 3/4 - inch meter - Commercial			
Tier One up to 10,000 Gallons	N/A	\$ 7.25	\$ 4.58
Tier Three - over 10,000 Gallons	N/A	\$ 8.69	\$ 5.49
One - inch meter- All			
Tier One up to 15,000 Gallons	N/A	\$ 7.25	\$ 4.58
Tier Two - over 15,000 Gallons	N/A	\$ 8.69	\$ 5.49
One and one half inch meter-All			
Tier One up to 20,000 Gallons	N/A	\$ 7.25	\$ 4.58
Tier Two - over 20,000 Gallons	N/A	\$ 8.69	\$ 5.49
Two - inch meter- All			
Tier One up to 25,000 Gallons	N/A	\$ 7.25	\$ 4.58
Tier Two - over 25,000 Gallons	N/A	\$ 8.69	\$ 5.49
Three - inch meter-All			
Tier One up to 70,000 Gallons	N/A	\$ 7.25	\$ 4.58
Tier Two - over 70,000 Gallons	N/A	\$ 8.69	\$ 5.49
Four - inch meter-All			
Tier One up to 250,000 Gallons	N/A	\$ 7.25	\$ 4.58
Tier Two - over 250,000 Gallons	N/A	\$ 8.69	\$ 5.49
Six - inch meter-All			
Tier One up to 800,000 Gallons	N/A	\$ 7.25	\$ 4.58
Tier Two - over 800,000 Gallons	N/A	\$ 8.69	\$ 5.49
Service Line and Meter Installation Charges			
5/8" x 3/4" Meter	N/A	\$ 520.00	\$ 385.00
3/4" Meter	N/A	\$ 600.00	\$ 385.00
1" Meter	N/A	\$ 690.00	\$ 435.00
1½" Meter	N/A	\$ 935.00	\$ 470.00
2" Meter - Turbine	N/A	\$1,595.00	\$ 630.00
2" Meter - Compound	N/A	\$2,320.00	\$ 630.00
3" Meter - Turbine	N/A	\$2,275.00	\$ 805.00
3" Meter - Compound	N/A	\$3,110.00	\$ 845.00
4" Meter - Turbine	N/A	\$3,520.00	\$ 1,170.00
4" Meter - Compound	N/A	\$4,475.00	\$ 1,230.00
6" Meter - Turbine	N/A	\$6,275.00	\$ 1,730.00
6" Meter - Compound	N/A	\$8,050.00	\$ 1,770.00
Service Charges			
Establishment	N/A	\$ 25.00	\$ 25.00
Establishment (After Hours)	N/A	\$ 35.00	\$ 35.00
Reconnection (Delinquent)	N/A	\$ 25.00	\$ 25.00
Reconnection (Delinquent) after hours	N/A	\$ 35.00	\$ 35.00
Meter Test (If Correct)	N/A	\$ 25.00	\$ 25.00
Deposit	N/A	*	*
Deposit Interest	N/A	*	*
Re-Establishment (Within 12 Months)	N/A	**	**
NSF Check	N/A	\$ 25.00	\$ 25.00
Deferred Payment	N/A	1.50%	1.50%
Meter Re-Read (If Correct)	N/A	\$ 10.00	\$ 10.00
Late Fee	N/A	1.00%	1.00%

\* Per Commission Rules (R14-2-403.B)

\*\* Months off system times the minimum (R14-2-403.D)

## TYPICAL BILL ANALYSIS

### Residential Service 3/4 - Inch Meter

Average Number of Customers: 5

<u>Company Proposed</u>	<u>Gallons</u>	<u>Present Rates</u>	<u>Proposed Rates</u>	<u>Dollar Increase</u>	<u>Percent Increase</u>
Average Usage	22,723	\$82.06	\$105.34	\$23.28	28.4%
Median Usage	7,750	\$31.15	\$42.12	\$10.97	35.2%

<u>Staff Recommend</u>					
Average Usage	22,723	\$82.06	\$126.06	\$44.00	53.6%
Median Usage	7,750	\$31.15	\$45.91	\$14.76	47.4%

### Present & Proposed Rates (Without Taxes) Residential Service 3/4 - Inch Meter

<u>Gallons Consumption</u>	<u>Present Rates</u>	<u>Company Proposed Rates</u>	<u>% Increase</u>	<u>Staff Proposed Rates</u>	<u>% Increase</u>
0	\$15.00	\$20.00	33.3%	\$15.00	0.0%
1,000	15.00	22.50	50.0%	18.05	20.3%
2,000	15.00	25.00	66.7%	21.10	40.7%
3,000	15.00	27.50	83.3%	24.15	61.0%
4,000	18.40	30.00	63.0%	28.73	56.1%
5,000	21.80	32.50	49.1%	33.31	52.8%
6,000	25.20	36.00	42.9%	37.89	50.4%
7,000	28.60	39.50	38.1%	42.47	48.5%
8,000	32.00	43.00	34.4%	47.05	47.0%
9,000	35.40	46.50	31.4%	51.63	45.8%
10,000	38.80	50.00	28.9%	56.21	44.9%
15,000	55.80	67.50	21.0%	83.66	49.9%
20,000	72.80	92.00	26.4%	111.11	52.6%
25,000	89.80	116.50	29.7%	138.56	54.3%
50,000	174.80	239.00	36.7%	275.81	57.8%
75,000	259.80	361.50	39.1%	413.06	59.0%
100,000	344.80	484.00	40.4%	550.31	59.6%
125,000	429.80	606.50	41.1%	687.56	60.0%
150,000	514.80	729.00	41.6%	824.81	60.2%
175,000	599.80	851.50	42.0%	962.06	60.4%
200,000	684.80	974.00	42.2%	1,099.31	60.5%

**TYPICAL BILL ANALYSIS**  
**COMMERCIAL Service 3/4 - Inch Meter**

Average Number of Customers: 8

<u>Company Proposed</u>	<u>Gallons</u>	<u>Present Rates</u>	<u>Proposed Rates</u>	<u>Dollar Increase</u>	<u>Percent Increase</u>
Average Usage	38,062	\$204.21	\$345.46	\$141.25	69.2%
Median Usage	10,929	\$111.96	\$129.93	\$17.97	16.1%

<u>Staff Recommend</u>	<u>Gallons</u>	<u>Present Rates</u>	<u>Proposed Rates</u>	<u>Dollar Increase</u>	<u>Percent Increase</u>
Average Usage	38,062	\$204.21	\$337.86	\$133.65	65.4%
Median Usage	10,929	\$111.96	\$188.90	\$76.94	68.7%

**Present & Proposed Rates (Without Taxes)**  
**COMMERCIAL Service 3/4 - Inch Meter**

<u>Gallons Consumption</u>	<u>Present Rates</u>	<u>Company Proposed Rates</u>	<u>% Increase</u>	<u>Staff Proposed Rates</u>	<u>% Increase</u>
0	\$85.00	\$50.70	-40.4%	\$138.00	62.4%
1,000	85.00	57.95	-31.8%	142.58	67.7%
2,000	85.00	65.20	-23.3%	147.16	73.1%
3,000	85.00	72.45	-14.8%	151.74	78.5%
4,000	88.40	79.70	-9.8%	156.32	76.8%
5,000	91.80	86.95	-5.3%	160.90	75.3%
6,000	95.20	94.20	-1.1%	165.48	73.8%
7,000	98.60	101.45	2.9%	170.06	72.5%
8,000	102.00	108.70	6.6%	174.64	71.2%
9,000	105.40	115.95	10.0%	179.22	70.0%
10,000	108.80	123.20	13.2%	183.80	68.9%
15,000	125.80	159.45	26.7%	211.25	67.9%
20,000	142.80	195.70	37.0%	238.70	67.2%
25,000	159.80	231.95	45.2%	266.15	66.6%
50,000	244.80	449.20	83.5%	403.40	64.8%
75,000	329.80	666.45	102.1%	540.65	63.9%
100,000	414.80	883.70	113.0%	677.90	63.4%
125,000	499.80	1,100.95	120.3%	815.15	63.1%
150,000	584.80	1,318.20	125.4%	952.40	62.9%
175,000	669.80	1,535.45	129.2%	1,089.65	62.7%
200,000	754.80	1,752.70	132.2%	1,226.90	62.5%

**TYPICAL BILL ANALYSIS**  
**COMMERCIAL Service 2 - Inch Meter**

Average Number of Customers: 1

<u>Company Proposed</u>	<u>Gallons</u>	<u>Present Rates</u>	<u>Proposed Rates</u>	<u>Dollar Increase</u>	<u>Percent Increase</u>
Average Usage	165,825	\$638.61	\$1,905.02	\$1,266.41	198.3%
Median Usage	165,825	\$638.61	\$1,905.02	\$1,266.41	198.3%
<u>Staff Recommend</u>					
Average Usage	165,825	\$638.61	\$2,312.63	\$1,674.02	262.1%
Median Usage	165,825	\$638.61	\$2,312.63	\$1,674.02	262.1%

**Present & Proposed Rates (Without Taxes)**  
**COMMERCIAL Service 2 - Inch Meter**

<u>Gallons Consumption</u>	<u>Present Rates</u>	<u>Company Proposed Rates</u>	<u>% Increase</u>	<u>Staff Proposed Rates</u>	<u>% Increase</u>
0	\$85.00	\$500.00	488.2%	\$1,425.00	1,576.5%
1,000	85.00	507.25	496.8%	1,429.58	1,581.9%
2,000	85.00	514.50	505.3%	1,434.16	1,587.2%
3,000	85.00	521.75	513.8%	1,438.74	1,592.6%
4,000	88.40	529.00	498.4%	1,443.32	1,532.7%
5,000	91.80	536.25	484.2%	1,447.90	1,477.2%
6,000	95.20	543.50	470.9%	1,452.48	1,425.7%
7,000	98.60	550.75	458.6%	1,457.06	1,377.7%
8,000	102.00	558.00	447.1%	1,461.64	1,333.0%
9,000	105.40	565.25	436.3%	1,466.22	1,291.1%
10,000	108.80	572.50	426.2%	1,470.80	1,251.8%
15,000	125.80	608.75	383.9%	1,493.70	1,087.4%
20,000	142.80	645.00	351.7%	1,516.60	962.0%
25,000	159.80	681.25	326.3%	1,539.50	863.4%
50,000	244.80	898.50	267.0%	1,676.75	584.9%
75,000	329.80	1,115.75	238.3%	1,814.00	450.0%
100,000	414.80	1,333.00	221.4%	1,951.25	370.4%
125,000	499.80	1,550.25	210.2%	2,088.50	317.9%
150,000	584.80	1,767.50	202.2%	2,225.75	280.6%
175,000	669.80	1,984.75	196.3%	2,363.00	252.8%
200,000	754.80	2,202.00	191.7%	2,500.25	231.2%

Note: This schedule is for illustrative purposes only. In fact, there is only one customer in this group with estimated usage of 165,825 gallons per month. The meter for this customer is broken.

## WIFA LOAN FINANCIAL ANALYSIS

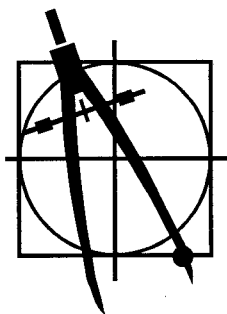
Test Year Income Statement, Capital Structure and Pro Forma Based on Audit  
Including Immediate Effects of the Proposed Debt

### INCOME STATEMENT

	<u>Test Year Ended December 31, 2006</u>	<u>Pro Forma</u>
Operating Revenue:	<b>\$31,828</b>	<b>\$66,400</b>
Operating Expenses:		
Purchased Water/Pumping Power	\$4,333	\$4,333
Admin. & General	25,408	24,513
Maintenance & Testing	778	1,499
Depreciation (d)	1,609	2,396
Property Taxes	2,922	2,922
Other taxes	0	0
Total Operating Expense	<u><b>\$35,050</b></u>	<u><b>\$35,663</b></u>
Pre-Tax Operating Income	<b>(\$3,222)</b>	<b>\$30,737</b>
Interest Income	\$0	\$0
Interest Expense (b)	<u>3,078</u>	<u>11,125</u>
Pre-Tax Net Income (a)	<u><b>(\$6,300)</b></u>	<u><b>\$19,612</b></u>
Principal Repayment (c)	2,014	6,454
Reserve/Replacement Deposit (e)	0	0
<b>TIER (Times Interest Earned Ratio)</b>		
(a) ÷ (b)	<b>N/M</b>	<b>1.76</b>
<b>DSC</b>		
[(a) + (d)] ÷ [(b) + (c)]	<b>N/M</b>	<b>1.25</b>

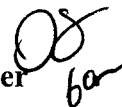
### CAPITAL STRUCTURE

Short-term Debt	\$2,014	2.3%	\$6,454	2.7%
Long-term Debt	\$48,959	56.9%	\$198,959	82.8%
Common Equity	\$34,997	40.7%	\$34,997	14.6%
Total Capital	\$85,970	100.0%	\$240,410	100.0%



**Engineering Report for:  
Picacho Peak Water Company  
for a Rate Increase  
Docket No. W-02351A-07-0686**

**By: Jian W Liu**  
**Utilities Engineer**

A handwritten signature in black ink, appearing to be 'JW Liu', written over the printed name.

**May 12, 2008**

**EXECUTIVE SUMMARY**

**CONCLUSIONS:**

1. A check with the Utilities Division Compliance Section showed no outstanding compliance issues for the Picacho Peak Water Company ("Picacho Peak" or "Company") (ACC Compliance Section Email dated 4/30/08).
2. The Company is located within the Arizona Department of Water Resources ("ADWR") Tucson Active Management Area ("AMA"), ADWR reported that the Company is in compliance with its monitoring and reporting requirements.
3. Staff concludes that the Picacho Peak Water system has adequate production capacity and storage capacity based on water use data for the year 2006 (see Section B of this report for further discussion).

**RECOMMENDATIONS:**

1. Staff recommends that the Company use the depreciation rates by individual National Association of Regulatory Utility Commissioners ("NARUC") category listed in Table B on a going forward basis.
2. Water testing expenses are based upon participation in the Arizona Department of Environmental Quality ("ADEQ") Monitoring Assistance Program. Annual testing expenses should be adjusted to \$1,499 as described in Table 1 (see Section F of this report for further discussion).
3. Staff recommends that the separate service line and meter installation charges developed by Staff and listed in Table C be approved (see Section K of this report for further discussion).

4. Staff recommends that within 90 days of a Decision in this matter the Company file with Docket Control, as a compliance item in this docket, documentation showing that the broken well meter has been fixed or replaced.
5. ADEQ has determined that the Picacho Peak water system, ADEQ Public Water System Identification No.11-038 (PWSID 11-038), is currently not delivering water that meets the water quality standards required by Arizona Administrative Code, Title 18, Chapter 4. (ADEQ Compliance Status Report dated 10/2/07, see Section C of this report for further discussion).
6. Picacho Peak signed a Consent Order with ADEQ dated May 2006. Staff recommends that the Picacho Peak file each January and July a report covering the previous six months that contains all activities regarding the ADEQ's Consent Order. The written report should continue until Staff receives notice that the Picacho Peak water system is in total compliance with ADEQ regulations.
7. Staff recommends that the Company file curtailment tariff in the form found on the Commission's website at:  
*<http://www.azcc.gov/Divisions/Utilities/forms/CurtailmentTariffSTANDARD.pdf>* This tariff shall be docketed as a compliance item in this case within 45 days of the effective date of an order in this proceeding for review and certification by Staff.
8. Staff recommends that the Company obtain information on Distribution Mains and report it in its next Annual Report (due April 2009).



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## **FIGURES**

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## A. LOCATION OF COMPANY

The Company's water system is located near Interstate 10 and Picacho Peak State Park in Pinal County and has a certificated area covering approximately 4 square miles. Figure 1 shows the location of Picacho Peak Water Company ("Picacho Peak" or "Company") within Pinal County and Figure 2 shows the certificated area.

## B. DESCRIPTION OF THE WATER SYSTEM

The plant facilities were visited on March 24, 2008, by Jian Liu, Staff Utilities Engineer, in the accompaniment of Gary Boileau, certified operator of the water system.

The facility follows a typical configuration found in small water systems. It consists of two wells, one 40,000 gallon storage tank, two pressure tanks and a distribution system. Figure 3 provides a process schematic for the water system. Staff concludes that the Picacho Peak Water system has adequate production capacity and storage capacity based on water use data for the year 2006.

### *(Tabular Description of Water System)*

#### Well Data

	Well No 2	Well No 1
ADWR ID No.	55-623405	55-623406
Casing Size	12 inch	12 inch
Casing Depth	350 ft	475 ft
Pump Size	10 Hp	10 Hp
Pump Yield	64 gal/min	82 gal/min

#### Storage, Pumping

Structure or equipment	Location	Capacity
booster pumps	Near Well Sites	One 10 HP and Two 7.5 HP
pressure tanks	Near Well Sites	One 5,000 & One 55 gallon
Storage tank	Near Well No 1	One 40,000 gallon

#### Distribution Mains

Diameter (inch)	Material	Length(ft)
2	Unknown	Unknown
3	Unknown	Unknown
4	Unknown	Unknown
6	Unknown	Unknown

Meters	
Size (inch)	Quantity
5/8 x 3/4	
3/4	13
1	
2	1

As can be seen above, no information is available for Distribution Mains. Staff recommends that the Company obtain this information and report it in its next Annual Report (due April 2009).

**C. ARIZONA DEPARTMENT OF ENVIRONMENTAL QUALITY COMPLIANCE (“ADEQ”)**

ADEQ has determined that the Picacho Peak water system, ADEQ Public Water System Identification No.11-038 (PWSID 11-038), is currently not delivering water that meets the water quality standards required by Arizona Administrative Code, Title 18, Chapter 4. (ADEQ Compliance Status Report dated 10/2/07).

ADEQ data base shows that this system has exceeded the Maximum Contaminant Level (“MCL”) for nitrate at Entry Point to the Distribution System (“EPDS”) #001 on 1-7-04, 6-7-06 and 2-28-07; this system has not installed the best available technology in accordance with R18-4-220 to achieve compliance with the MCL. By exceeding the MCL, this system has triggered increased monitoring from annual to quarterly and has subsequently failed to provide increased quarterly monitoring.

ADEQ data base shows that this system has exceeded the MCL for total Coliform on 5-2-07 and 6-6-07.

ADEQ data base does not show that the required initial two consecutive six month lead and copper monitoring has been completed. This system is required to provide ten samples for two consecutive six month monitoring periods but has only provided 5 samples taken on July 7, 2004.

Picacho Peak signed a Consent Order with ADEQ dated May 2006. Staff recommends that the Picacho Peak file each January and July a report covering the previous six months that contains all activities regarding the ADEQ’s Consent Order. The written report should continue until Staff receives notice that the Picacho Peak water system is in total compliance with ADEQ regulations.

**D. ARIZONA CORPORATION COMMISSION ("ACC") COMPLIANCE**

A check with the Utilities Division Compliance Section showed no outstanding compliance issues. (ACC Compliance Section Email dated 4/30/08)

**E. ARIZONA DEPARTMENT OF WATER RESOURCES ("ADWR") COMPLIANCE**

The Company is located within the Tucson Active Management Area ("AMA") and the ADWR reported that the Company is in compliance with its monitoring and reporting requirements.

**F. WATER TESTING EXPENSES**

The Company is subject to mandatory participation in the Monitoring Assistance Program ("MAP"). Starting January 1, 2002, water companies paid a fixed \$250 per year fee, plus an additional fee of \$2.07 per service connection regardless of meter size for participation in MAP. Participation in the MAP program is mandatory for water systems, which serve less than 10,000 persons (approximately 3,300 service connections).

The Company reported its water testing expense at \$1,044 during the 2006 test year. Staff has reviewed the Company's testing expense and has recalculated the testing costs. Table 1 shows Staff's annual monitoring expense estimate of \$1,499 with participation in the MAP.

**Table 1 Water Testing Cost**

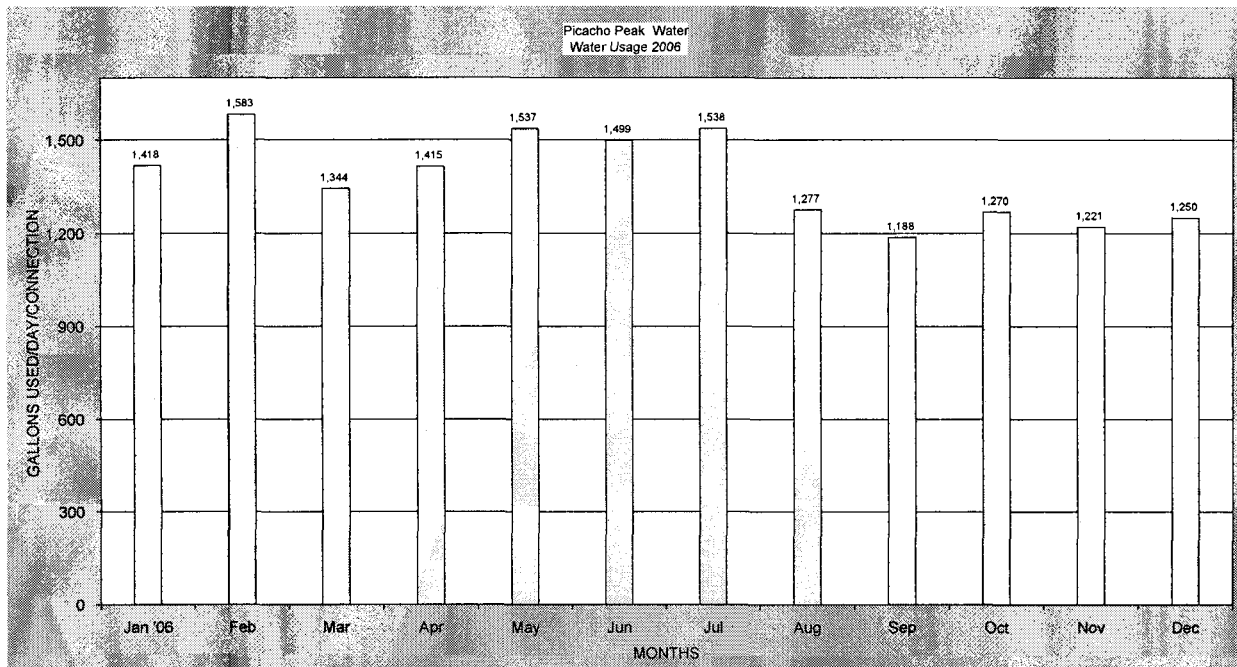
Monitoring – 2 wells (Tests per 3 years, unless noted.)	Cost per test	No. of tests per 3 years	Total 3 year cost	Annual Cost
Bacteriological – monthly	\$30	36	1080	360
Inorganics – Priority Pollutants	\$480	1	480	160
Gross Alpha	\$110	4	440	110
Nitrate - quarterly	\$50	12	600	200
Nitrite – once per period	\$30	1	30	10
Asbestos – per 9 years	\$360	1	120	40
MAP – IOCs, SOCs, & VOCs	MAP	MAP	MAP	286
Lead & Copper - annual	\$50	20	1000	333
Total				<b>\$1,499</b>

Staff recommends annual water testing expense of \$1,499 be used for purposes of this application.

## G. WATER USE

### Water Sold

Based on the information provided by the Company, water use for the year 2006 is presented below. The high monthly domestic water use was 1,583 gal/day per service connection in February and the low monthly domestic water use was 1,188 gal/day per service connection in September. The average annual use was 1,378 gal/day per service connection. The high average and median water use can be attributed to the fact that this system has 9 commercial customers and only 5 residential customers.



### Non-account Water

Non-account water should be 10% or less and never more than 15%. It is important to be able to reconcile the difference between water sold and the water produced by the source. A water balance will allow a water company to identify water and revenue losses due to leakage, theft, and flushing. The Company did not report gallons pumped for 2006 because the well meter was broken.

Staff recommends that within 90 days of a Decision in this matter the Company file with Docket Control, as a compliance item in this docket, documentation showing that the broken well meter has been fixed or replaced.

#### **H. GROWTH**

The Company reported no growth in service connections for the two-year period between 2004 and the test year 2006. Therefore, Staff s expects that the Company will have little or no growth in the foreseeable future.

#### **I. DEPRECIATION RATES**

Staff recommends that the Company use the depreciation rates by individual National Association of Regulatory Utility Commissioners ("NARUC") category listed in Table B on a going forward bases.

Table B. Depreciation Rates

NARUC Acct. No.	Depreciable Plant	Average Service Life (Years)	Annual Accrual Rate (%)
304	Structures & Improvements	30	3.33
305	Collecting & Impounding Reservoirs	40	2.50
306	Lake, River, Canal Intakes	40	2.50
307	Wells & Springs	30	3.33
308	Infiltration Galleries	15	6.67
309	Raw Water Supply Mains	50	2.00
310	Power Generation Equipment	20	5.00
311	Pumping Equipment	8	12.5
320	Water Treatment Equipment		
320.1	Water Treatment Plants	30	3.33
320.2	Solution Chemical Feeders	5	20.0
330	Distribution Reservoirs & Standpipes		
330.1	Storage Tanks	45	2.22
330.2	Pressure Tanks	20	5.00
331	Transmission & Distribution Mains	50	2.00
333	Services	30	3.33
334	Meters	12	8.33
335	Hydrants	50	2.00
336	Backflow Prevention Devices	15	6.67
339	Other Plant & Misc Equipment	15	6.67
340	Office Furniture & Equipment	15	6.67
340.1	Computers & Software	5	20.00
341	Transportation Equipment	5	20.00
342	Stores Equipment	25	4.00
343	Tools, Shop & Garage Equipment	20	5.00
344	Laboratory Equipment	10	10.00
345	Power Operated Equipment	20	5.00
346	Communication Equipment	10	10.00
347	Miscellaneous Equipment	10	10.00
348	Other Tangible Plant	----	----

NOTES:

1. These depreciation rates represent average expected rates. Water companies may experience different rates due to variations in construction, environment, or the physical and chemical characteristics of the water.
2. Acct. 348, Other Tangible Plant may vary from 5% to 50%. The depreciation rate would be set in accordance with the specific capital items in this account.

**J. CURTAILMENT PLAN TARIFF**

A Curtailment Plan Tariff ("CPT") is an effective tool to allow a water company to manage its resources during periods of shortages due to pump breakdowns, droughts, or other unforeseeable events. Since the Company does not have this type of tariff, this proceeding provides an opportune time to prepare and file such a tariff.

Staff recommends that the Company file curtailment tariff in the form found on the Commission's website at:

<http://www.azcc.gov/Divisions/Utilities/forms/CurtailmentTariffSTANDARD.pdf> This tariff shall be docketed as a compliance item in this case within 45 days of the effective date of an order in this proceeding for review and certification by Staff.

**K. METER AND SERVICE LINE INSTALLATION CHARGES**

The Company proposed changes to its existing service line and meter installation charges which are listed in Table C below. Service line and meter installation charges are refundable advances and the Company's proposed charges are within Staff's recommended range for these charges. Since the Company may at times install meters on existing service lines, it would be appropriate for some customers to only be charged for the meter installation. Therefore, separate service line and meter installation charges have been developed by Staff. Staff recommends that the Company use the separate service line and meter installation charges developed by Staff. The separate service line charges and meter charges recommended by Staff and listed in Table C equal the Company's total proposed charge.



Table C. Service Line and Meter Installation Charges

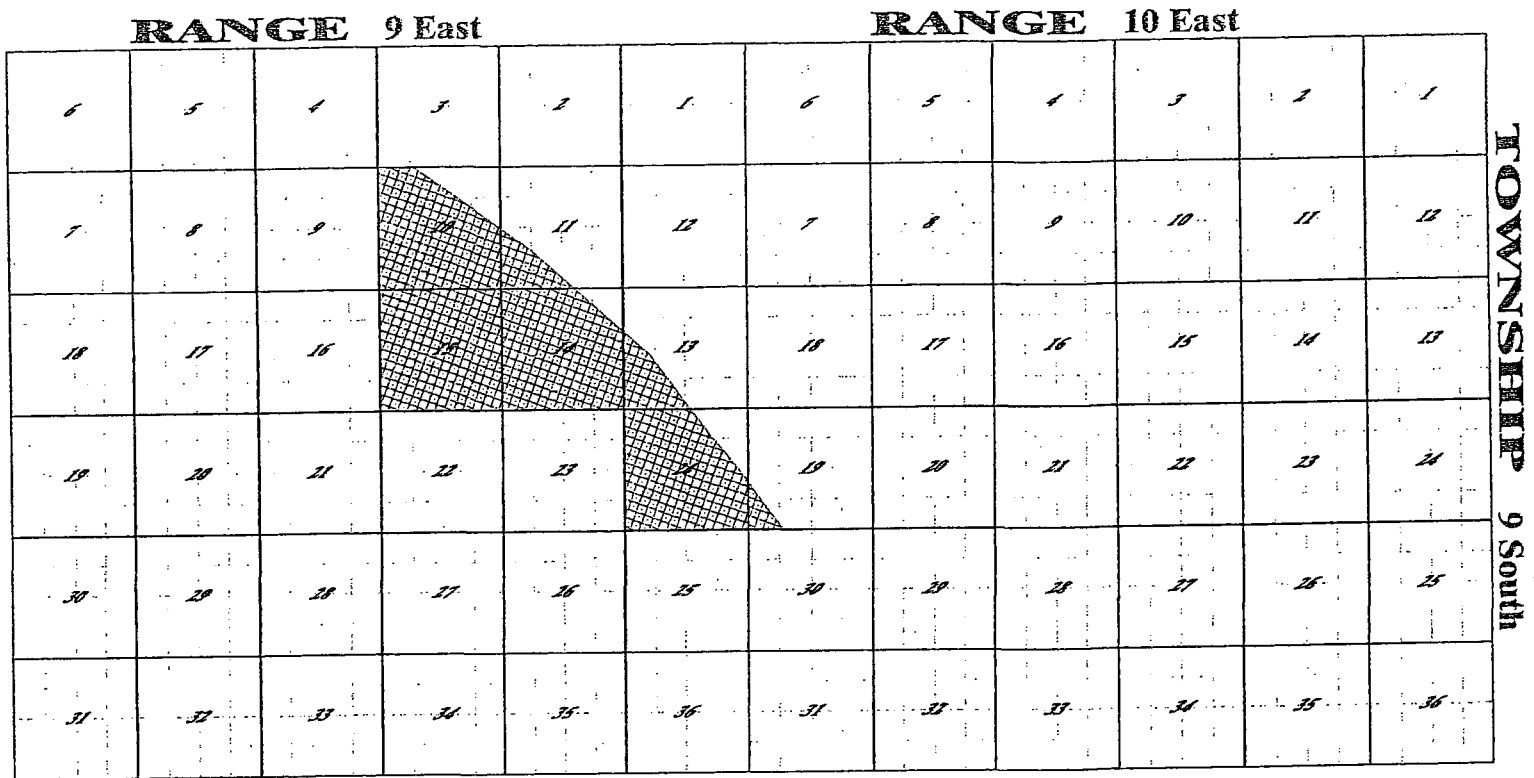
Meter Size	Proposed Charges	Staff recommended service line charges	Staff recommended meter charges	Staff recommended Total Charges
5/8 x3/4-inch	\$520	385	135	\$520
3/4-inch	\$600	385	215	\$600
1-inch	\$690	435	255	\$690
1-1/2-inch	\$935	470	465	\$935
2-inch - Turbine	\$1595	630	965	\$1595
2-inch - Compound	\$2320	630	1690	\$2320
3-inch - Turbine	\$2275	805	1470	\$2275
3-inch - Compound	\$3110	845	2265	\$3110
4-inch - Turbine	\$3520	1170	2350	\$3520
4-inch - Compound	\$4475	1230	3245	\$4475
6-inch - Turbine	\$6275	1730	4545	\$6275
6-inch - Compound	\$8050	1770	6280	\$8050

[illegible]

- |       |                                      |       |   |
|-------|--------------------------------------|-------|---|
| 1445  | ARIZONA WATER COMPANY                | 2351  | PICACHO PEAK WATER COMPANY              |
| 20496 | AVM-2005, LLC                        | 3528  | PICACHO WATER COMPANY                   |
| 2026  | BIDEGAIN WATER COMPANY               | 1774  | PICACHO WATER IMPROVEMENT CORPORATION   |
| 2721  | CARTER WATER COMPANY                 | 1395  | QUEEN CREEK WATER COMPANY               |
| 3847  | CASA GRANDE SOUTH WATER COMPANY      | 4245  | RED ROCK UTILITIES, LLC                 |
| 1990  | CASA GRANDE WEST WATER COMPANY, INC. | 3861  | RIDGEVIEW UTILITY COMPANY               |
| 2442  | CP WATER COMPANY                     | 3576  | SANTA CRUZ WATER COMPANY                |
| 2859  | DIVERSIFIED WATER UTILITIES, INC.    | 4137  | SANTA ROSA WATER COMPANY                |
| 1775  | FRANCISCO GRANDE UTILITY COMPANY     | 2485  | SPRING BRANCH WATER COMPANY, INC.       |
| 2497  | GOLDEN CORRIDOR WATER COMPANY        | 4015  | SUNLAND WATER COMPANY                   |
| 2500  | GOODMAN WATER COMPANY                | 2425  | SUN VALLEY FARMS, UNIT VI WATER COMPANY |
| 2234  | H2O, INC.                            | 3230  | TWIN HAWKS UTILITY, INC.                |
| 2258  | HACIENDA ACRES WATER SYSTEM          | 1993  | UNITED UTILITIES                        |
| 2987  | JOHNSON UTILITIES COMPANY            | 20432 | WILLOW SPRINGS UTILITIES, LLC           |
| 1944  | LAGO DEL ORO WATER COMPANY           | 4264  | WOODRUFF WATER COMPANY, INC.            |
| 2353  | PARK WATER COMPANY                   |       |   |

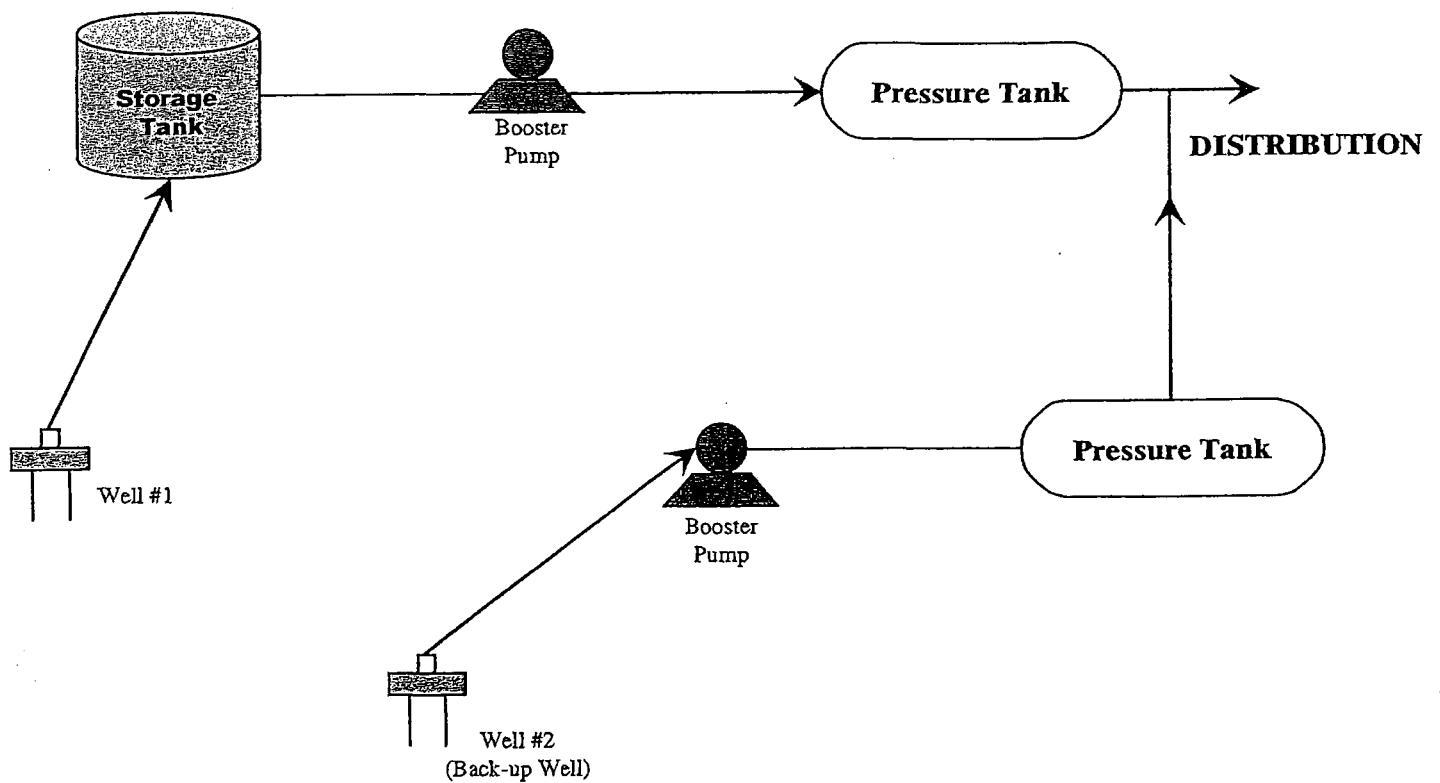
### Figure 1: Pinal County Map

# COUNTY: *Pinal*



 W-2351 (2)  
 Picacho Peak Water Company

**Figure 2: Certificated Area**




**Figure 3. Process Schematic**

**MEMORANDUM**

DATE: May 12, 2008

TO: Gerald Becker  
Public Utilities Analyst V  
Utilities Division

FROM: Jian W. Liu   
Utilities Engineer  
Utilities Division

RE: Picacho Peak Water Company, Inc.  
Docket No. W-02351A-07-0319 (Financing)

---

**Introduction**

Picacho Peak Water Company ("Picacho Peak" or "Company") is located near Interstate 10 and Picacho Peak State Park in Pinal County with a certificated area covering approximately 4 square miles. The Company presently provides utility service to approximately 5 residential customers and approximately 9 commercial customers in portions of Pinal County, Arizona.

**Financing Application**

On May 22, 2007, the Company filed an application with the Arizona Corporation Commission ("Commission") requesting authority to incur debt to finance water system improvements. On December 13, 2007, Picacho Peak amended its finance application to incorporate proforma adjustments to the previously submitted balance sheet and income statements.

**Engineering Analysis**

In May 2006, an Arizona Department of Environmental Quality ("ADEQ") Consent Order was issued for Picacho Peak which outlined a plan to bring the Company into full compliance with ADEQ regulations. Water quality testing has shown that the nitrate level in the Company's source water exceeds federal standards.

The primary purpose of this finance application is to receive authority to borrow \$150,000 from the Water Infrastructure Finance Authority of Arizona ("WIFA") to purchase and install treatment facilities.

Picacho Peak plans to install reverse osmosis systems at specific points where drinking water is most likely dispensed.

Staff concludes that the proposed reverse osmosis systems are appropriate.

### **Cost Analysis**

The Company and ADEQ have agreed that the most economically feasible plan is to install reverse osmosis systems at specific points where drinking water is most likely dispensed. The Company needs the WIFA loan to hire an engineer to develop the work plan and determine the exact treatment plant size, location, and capacity for each customer.

The Company has estimated that it will need \$150,000 to construct adequate treatment. The Company based this estimate upon general discussions it has had with ADEQ staff, consulting engineers, and vendors of the treatment equipment. Since the Company does not have a detailed construction work plan it is difficult to determine if this cost estimate is reasonable. Based on the available information, Staff concludes that the proposed cost estimate is a good starting point.

### **Conclusion**

Staff concludes that the proposed plant additions are reasonable and appropriate. However, no "used and useful" determination of the proposed plant was made, and no particular future treatment should be inferred for rate making or rate base purposes.